Supreme Court, U.S.
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No. 96-577

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1996

TRISTAR CORPORATION,

Petitioner,

v.

ROSS A. FREITAS and CAROLYN SAFER KENNER,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION OF RESPONDENTS

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CORRECT DENOMINATION OF NAMES

Respondents, defendants below, are Ross A. Freitas and Carolyn Safer Kenner (incorrectly spelled *Caroline* Safer Kenner on the cover of Petitioner's petition).

Each of the respondents join in this brief in opposition.

Respondents' attorneys below (following Respondents' pro-se representation) were Caro & Graifman, P.C., by Chase A. Caro and Brian D. Graifman (incorrectly denominated by Petitioner, *compare* Pet. App. 2 *with* 84 F.3d 550, 551 (2d Cir.), *reh'g denied* (1996)).

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COUNTER-STATEMENT OF THE CASE

A. Section 16

Section 16(b) of the Securities Exchange Act permits a shareholder or issuer to maintain action against any director, officer or beneficial owner of more than 10% of any class of outstanding shares (a "statutory insider") who profits from short-swing transactions in that corporation's securities. 15 U.S.C. 78p(b). A short-swing transaction is "any purchase and sale, or any sale and purchase, of any equity security of such issuer . . . within any period of less than six months." *Id.* A suit to recover such profits may be brought "by the issuer, or by the owner of any security of the issuer . . . in behalf of the issuer . . . ; *but no such suit shall be brought more than two years after the date such profit was realized.*" *Id.* (emphasis added).

Section 16(a) provides a mechanism for facilitating the recovery of short-swing profits by requiring statutory insiders to disclose any change in ownership "within ten days after the close of each calendar month" in which such change occurs. *Id.* § 78p(a). That disclosure is made via a Form 4 or Form 5 (filed with the Commission and made publicly available). The corporation or shareholder may then use the Forms to establish liability in an action under section 16(b). Because the "statute imposes liability without fault within its narrowly drawn limits," *Foremost-McKesson, Inc. v. Provident Secs. Co.*, 423 U.S. 232, 251 (1976), recovery in such actions "is virtually automatic." *Whittaker v. Whittaker Corp,* 639 F. 2d 516, 522 (9th Cir.), *cert. denied,* 454 U.S. 1031 (1981).

Section 16(b), instituted as a strict liability provision, is necessarily arbitrary. Accordingly, fraudulent minded

insiders are treated identically to those with the best intentions. However, unlike most provisions in the Exchange Act, section 16(b) is not a criminal provision. It does not make short-swing trading illegal. Instead, the section merely provides that the profits from certain trades essentially belong to the issuer.

B. Brief Factual Background

From 1982 through at least May 31, 1989, Respondents served as officers and directors of Ross Cosmetics and were beneficial owners of more than ten percent of the outstanding shares of the company's common stock. In separate transactions occurring in February through June 1989, the Respondents purchased more than 39,000 shares of Ross Cosmetics at prices ranging from $1.10 to $4.50 per share.

On May 31, 1989, the Respondents entered into a binding contract (the "Agreement") to sell to Starion International Limited ("Starion") a total of 906,594 shares of Ross Cosmetics common stock, approximately 28 percent of the company's outstanding shares. The Agreement required the Respondents to transfer the shares to Starion in more than a dozen installments. In return, the Respondents were to receive "loan disbursements" fixed at between approximately $4.65 and $7.50 for each share in each installment. Through this transaction (and others), Starion acquired control of Ross Cosmetics, which was later re-named Tristar (the Petitioner herein).

The transaction represented by the May 31, 1989 Agreement was required by Section 16(a) to be disclosed through the Securities Exchange Commission (the "Commission") on or before June 10, 1989 in a Form 4

filing. *See* 17 C.F.R. § 240.16a-3(a) (1995) (addressing forms). The Respondents, however, did not file a Form 4 until December 18, 1991. On December 16, 1993, Tristar filed its complaint pursuant to Section 16(b) of the Securities Exchange Act to recover the Respondents' short-swing profits.

C. Course of Proceedings and Disposition Below

On July 20, 1994, Tristar moved for summary judgment. In an opinion dated November 9, 1994, the district court determined that the Agreement constituted a "sale" of securities as defined by Section 3 of the Securities Exchange Act, 15 U.S.C. § 78c(a)(14). *Tristar Corp. v. Freitas*, 867 F. Supp. 149, 152-53 (E.D.N.Y. 1994) (Pet. App. 17-19). The court also found that the Respondents had reaped short-swing profits by entering into the Agreement with Starion, giving rise to a cause of action that accrued on May 31, 1989. *Id.* But because the two year period of limitations set forth in Section 16(b) expired on May 31, 1991, the district court found that Tristar's complaint (filed on December 16, 1993) would be, absent tolling, "clearly untimely." *Id.* at 153 (Pet. App. 19).

Nevertheless, the district court found that Tristar was entitled to equitable relief, and tolled the running of the limitations period for more than two and one half years, since the Agreement entered into on May 31, 1989 (an agreement to which the Petitioner is a party) was not disclosed until December 18, 1991. The district court, relying on the Ninth Circuit decision in Whittaker, held that Section 16(b)'s two-year period of limitation was equitably tolled during the Respondents' delinquency. The district court thus determined that the two-year limitations period began to run on the date that the Respondents filed their Form 4 (Dec. 18, 1991).

Accordingly, the Petitioner met the two-year limitations period by filing its complaint on December 16, 1993, two days before the limitation expired. *Id.* at 153-54 (Pet. App. 19-21).

The Second Circuit Court of Appeals reversed, finding that the Petitioner's complaint was not filed within the limitations period. 84 F.3d 550 (2d Cir.), *reh'g denied* (1996) (Pet. App. 1-9). Assuming arguendo that equitable tolling would be appropriate, the court opined that the limitations period began to run from the time that the short-swing profits were realized (May 31, 1989), and could not be tolled until the required Section 16(a) filing became untimely -- here, on the tenth calendar day of the month following the transaction, or June 10, 1989. At that point in time, the limitations period would be tolled until the required disclosure was made (Dec. 18, 1991). The limitations period would then continue to run again, after the filing has been made. Thus, counting from the disclosure (Dec. 18, 1991), the limitation period would run two years (Dec. 18, 1993), minus those 10 days between the profit realization date and the date respondents' delinquency began and the necessary form should have been filed, or December 8, 1993. Since Tristar's complaint was not filed until December 16, 1993, it was untimely and correctly was dismissed.

It is important to note that the Second Circuit did not rule on whether it was appropriate to grant equitable tolling in this case. As the Second Circuit noted at Footnote 2:

> On June 5, 1989, Ross Cosmetics filed a Form 8-K (which is required to be filed when a change of control of the registrant occurs, see 17 C.F.R. § 249.308 (1995)) with the Commission

> disclosing the Agreement. There is therefore record evidence that Tristar -- which, as noted, is controlled by Starion, the same entity that purchased the defendant's shares -- had actual and contemporaneous notice of the defendant's short-swing profits. However, because we hold that Tristar's complaint would not be timely even if the limitations period were tolled, we need not decide whether Tristar's putative knowledge renders the equitable tolling doctrine inapplicable

84 F.3d at 553-54 n.2 (Pet. App. 8 n.2).

REASONS FOR DENYING THE PETITION

I. The "conflict" is illusory.

Although Petitioner postures the decision below as in direct conflict with *Whittaker v. Whittaker Corp.*, 639 F.2d 516 (9th Cir.), *cert. denied*, 454 U.S. 1031 (1981) (Pet. App. 35-77), a careful review of the facts of both cases illustrates that there really is no such conflict. This is so because applying the rule set forth by the Second Circuit here to the facts in *Whittaker* would not change the results there one iota.

In *Whittaker*, the relevant trading period was between December 1, 1965 and December 31, 1970. 639 F.2d at 518 (Pet. App. 37). The district court had cut off liability for transactions prior to January 29, 1969, two years prior to

when demand was made for recovery of short-swing profits. *Id.* at 519 (Pet. App. 37).

Significantly, however, reports of the transactions in question there had never been filed. *Id.* at 534 (Pet. App. 77). For that reason, the Ninth Circuit found that the running of any limitations period would be tolled (and would not begin to run until disclosed) and recovery could be had for the short-swing profits arising from trades in the full relevant trading period. *Id.*

Using the Second Circuit's *Tristar* rule, the limitations period in *Whittaker* would similarly be tolled (at least under the rule the Second Circuit accepted arguendo) until the disclosure (which never occurred in *Whittaker*). The only period of *Whittaker* where the running of the limitations period would not be tolled under the Second Circuit interpretation would be that period between each individual short-swing transaction and the time it should have been disclosed -- a maximum of 40 days, not enough to exhaust the two-year limitations period.

Accordingly, there are facts and issues critical here that were not present in *Whittaker*, and the Court there did not have reason to confront the issue that the Second Circuit confronted here. Any implication that the Petitioner seeks to extract from *Whittaker* arises from mere dictum. Cases, however, are decided on facts, not slogans, and comparing the facts here to those in *Whittaker* reveals there is no circuit conflict.

II. The issue is not an important issue of federal law that must be decided by this Court.

An additional reason this Court need not consider the issue is that it is not an important issue of federal law that must be decided by this Court. Apparently, only two federal circuits -- the Second and Ninth -- have arguably addressed this issue. In the over sixty (60) years since the enactment of Section 16(b), only a handful of cases are relevant to the issue at hand, and there is no reason to believe that there will be any material increase in the number of cases confronting this issue and requiring guidance by this Court.

III. The decision below is consistent with congressional intent and not inconsistent with any decision of this court.

Additionally, the decision of the Second Circuit is consistent with the intent of Congress and not inconsistent with any decision of this Court.

Section 16(b) states quite plainly that "[n]o such suit shall be brought more than two years after the date such profit was realized." Not insignificantly, this language occurs in the same sentence that grants jurisdiction and provides the authorization for the institution of such suits. Thus, the two-year limit provided within this clause would seem jurisdictional in nature. *See, e.g. Hardin v. City Title*, 797 F.2d 1037 (D.C. Cir.) (unanimous opinion of Scalia, Bork & MacKinnon, J.J.) (time limitation as integral part of jurisdictional clause).

In addition, this statute creates a cause of action in derogation of common law, and therefore must be narrowly construed. If tolling would apply, it therefore must be

done so to the minimal extent possible. Indeed, here, where Petitioner waited more than four years after the transaction (of which it had actual knowledge), tolling would be inequitable. *See Cada v. Baxter Healthcare Corp.*, 920 F.2d 446 (7th Cir. 1990) (Posner, Easterbrook, Wood, JJ.) (where plaintiffs do not need tolling, not equitable to give it).

Petitioner nevertheless argues that application of the rule set forth by the Second Circuit would lead to "confusion," "lack of uniformity" and "anomalous results" arising out of varying reporting requirements that the court below overlooked (Pet. 8-12). Petitioner's parade of horribles, however, falls flat. There is nothing confusing or unduly variable about the rule the Second Circuit applies or the result here. Respondents' eventual disclosure --even ignoring the initial disclosure on the Form 8K, contemporaneous with the Agreement constituting the transaction -- set forth the date of the transaction, following from which it would be quite simple to determine the date on which the event should have been disclosed, and therefore to calculate the date the limitations period would expire should tolling apply.

The fact that in some limited circumstances reports may *timely* be filed until up to 45 days after the issuer's fiscal year -- which Petitioner argues would effectively reduce the period in which a party might be able to react to a short-swing profit -- is no reason to eschew the rule applied here. If the insider can await that later date *legally* without disclosing the transaction, then there is no good reason why that period should count against the insider. In such a case, there is still ample time for a party to seek to recover the short-swing profits. Petitioner would shamelessly rewrite the rule so as to directly and drastically vary it from the language Congress used.

Nor is the rule here inconsistent with *Lampf, Pleva, Lipkind, Prupis, & Petigrow v. Gelbertson*, 501 U.S. 350 (1991), as Petitioner suggests (Pet. 9 n.1). There is absolutely nothing in *Lampf* (which applied a 1-year/3-year period to Section 10(b) and Rule 10b-5) that compels a result different from the one here. *Lampf* involved a statute with no express limitations period, whereas the statutory provision at issue here, Section 16(b), *does* have an express limitations period.

In fact, a proper reading of *Lampf* compels affirming the result here. This Court in *Lampf*, distinguishing between discovery periods and periods of repose (such as the 1-year/3-year period found applicable there), referred specifically to the two-year period in Section 16(b) as a "period of repose." 501 U.S. 350 at 360 n.5. Whereas a statute of limitation extinguishes a right to prosecute a cause of action from the time it accrues, a statute of repose confines potential liability by limiting time during which a cause of action can arise and terminates the right of action, regardless of the time of accrual of the cause of action or of notice to plaintiff of the invasion of legal rights. See Black's Law Dictionary 927 & 1411 (6th ed. 1990). In other words, the two-year limit is an outer limit, such as the 3-year portion of the period in *Lampf*, and not subject to equitable tolling. *See Lampf*, 501 U.S. at 363 ("[t]he 3-year limit is a period of repose inconsistent with tolling"; "an outside limit"; "clearly to serve as a cutoff"; "tolling principles do not apply").

Moreover, resolving the issue at hand will not change the result, because equitable tolling is improper in this case in any event (*see* discussion, *supra*). *See also* ABA Committee on Federal Regulation of Securities, Report of the Task Force on Statute of Limitations for Implied Actions 645, 655 (1986) (advancing "the inescapable conclusion that

Congress did not intend equitable tolling to apply in actions under the securities laws"), *cited with approval in Lampf*, 501 U.S. at 363.

IV. The issue of dates of the matchable purchases and sales is not properly before this Court because petitioner failed to raise it before the Court below on appeal, and in any event the issue is irrelevant to the analysis.

The Petitioner presents the Court with a "red herring" argument regarding the Second Circuit's method of calculating "matchable" purchases and sale by the insider (Pet. 14-15). As an initial matter, however, this issue was not preserved for review. As the Second Circuit noted, "No appeal is taken from the district court's finding that short-swing profits were 'realized' on the date that the Agreement was entered into -- May 31, 1989 -- and therefore that Tristar's claim accrued on that date." 84 F.3d at 553 (Pet. App. 7). The realization date, of course, is the date the period of limitations would begin to run under Section 16(b), 15 U.S.C. § 78p(b).

In any event, regardless of whether the court uses the May 31, 1989 Agreement as the profit realization date or the June 1989 purchases, the outcome would be the same under the Second Circuit's method of calculation. Under the Second Circuit interpretation (assuming arguendo that tolling is proper), the limitations period would begin running from the period of the June transaction (depending on the date of transaction) until July 10, the last day the Form 4 could have been timely filed for those purchases -- a period of between 10 and 39 days. Hence, between 10 and 39 days (not ten days as with the May 31, 1989 Agreement) would have passed and the period would have restarted upon the filing

with the Commission on December 18, 1991. Considered from December 18, 1991 (the date of the Form 4 filing), a period of two years, minus the ten to thirty-nine days would have already passed during which the limitations period was running, resulting in the period expiring prior to December 16, 1993, when Petitioner brought suit.[1]

Accordingly, the appeals court overlooked nothing on this issue, and properly decided this case and declined Petitioner's request for rehearing or in the alternative for rehearing in banc.

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[1] Similarly, under the "Ninth Circuit" interpretation Petitioner presses, there would be no difference in result than with the May 31, 1989 realization date because (by Petitioner's view) under both scenarios the limitations period would begin running from the December 18, 1981 date of Form 4 filing.

CONCLUSION

The writ of certiorari should be denied.

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